



# Audit Report



OIG-07-038

SAFETY AND SOUNDNESS: OCC Could Further Strengthen Its Ability to Assess Risks to Community Banks Following Emergencies

May 25, 2007

Office of  
Inspector General

Department of the Treasury



# Contents

---

Audit Report..... 3

Results in Brief ..... 3

Background ..... 5

Findings and Recommendations ..... 8

Improvements Could be Made to OCC’s Guidance to Assess the Financial  
Condition of At Risk Community Banks Following Emergencies ..... 9

Recommendations..... 11

Improvements Could be Made to OCC’s Operational Assessment Process for  
Community Banks Following Emergencies..... 12

Recommendations..... 15

## Appendices

Appendix 1: Objectives, Scope, and Methodology ..... 17

Appendix 2: Management Response ..... 18

Appendix 3: Major Contributors to This Report..... 21

Appendix 4: Report Distribution..... 22

## Abbreviations

CAMELS	Capital, Assets, Management, Earnings, Liquidity, Sensitivity to risk
COOP plan	Continuity of Operations plan
FDIC	Federal Deposit Insurance Corporation
FFIEC	Federal Financial Institutions Examination Council
FRB	Board of Governors of the Federal Reserve System
NCUA	National Credit Union Administration
OIG	Office of Inspector General
OCC	Office of the Comptroller of the Currency
OTS	Office of Thrift Supervision
Treasury	Department of the Treasury

---

**This page intentionally left blank.**

---

*The Department of the Treasury  
Office of Inspector General*

May 25, 2007

John C. Dugan  
Comptroller  
Office of the Comptroller of the Currency

During the 2005 hurricane season, Hurricanes Katrina and Rita struck states along the Gulf of Mexico, causing major destruction and disruption in portions of Alabama, Louisiana, Mississippi, and Texas. Following these hurricanes, we conducted an audit to determine (1) how prepared the Office of the Comptroller of the Currency (OCC) was to address the needs of national banks and their customers during and immediately following the hurricanes and (2) OCC's plans and abilities to assess and manage increased risks to national banks following the hurricanes. We focused our audit on OCC's supervision of community banks because, with the exception of one large bank and one midsize bank, all affected banks determined to be at risk by OCC were community banks.

## **Results in Brief**

OCC determined that Hurricanes Katrina and Rita had posed risks to community banks in the Gulf Coast Region. Short term, the risks were primarily to the banks' operations, while long term risks were primarily to the banks' financial condition. OCC evaluated these risks by obtaining assessments from bank management and subsequently performing analyses and examinations.

OCC obtained initial financial information on at risk community banks within 45 days after Hurricane Katrina and 19 days after Hurricane Rita. We found that OCC could improve its

---

procedures to assess the financial condition of at risk<sup>1</sup> community banks following emergencies as:

- OCC Emergency Event Procedures did not specifically address documenting all important elements of financial condition from at risk community banks in a consistent manner.
- OCC did not specify timeframes for analyzing the effects of the hurricanes on the at risk community banks' financial condition.

We also found areas where OCC could improve its operational risk assessment of community banks following emergencies as:

- OCC could not provide evidence of contact with all community banks in areas affected by Hurricane Rita and weaknesses existed in the identification of banks in these areas.
- OCC had difficulty establishing communication with community banks following Hurricane Katrina.

We are recommending that OCC: (1) modify its Emergency Event Procedures to require documentation and summarization of all important elements of financial condition for at risk community banks in a consistent manner; (2) modify its Emergency Event Procedures to require that following such an event, OCC determine timeframes for analyzing the effects on at risk community banks financial condition, based on the gravity of the situation; (3) document its contact made with individual banks following an emergency event and develop a methodology to accurately identify banks to be monitored in emergency events; and (4) maintain alternative contact information for bank personnel.

While OCC agreed to address our recommendations, it expressed a concern that the report may give the impression that OCC did not take appropriate responsive action to Hurricanes Katrina and Rita, as opposed to not fully document its action. Our report did focus more on improvements in

---

<sup>1</sup> OCC categorized 12 community banks at risk based on their lending exposure in areas most affected by the hurricanes.

---

documentation rather than actions taken by OCC, as the documentation we reviewed did not allow for a clear determination of when elements of the condition of at risk banks were established. OCC also stated that at no time was it unaware of either storm's effect on its institutions, their markets, or their communities. However, OCC did not fully demonstrate its awareness of each storm's effect.

OCC has agreed to modify its Emergency Event Procedures to incorporate its risk based approach to supervision. To the extent that the modification to the procedures leads to documentation and summarization of the financial condition of at risk banks and addresses the establishment of timeframes after disasters, the corrective action will be responsive to recommendations (1) and (2). OCC's conveyance to its senior district management of its belief that documentation of significant events could be improved does not address the need to better identify banks included in recommendation (3). OCC's agreement to ensure their systems include alternative contact information for bank personnel is responsive to recommendation (4).

## Background

Hurricane Katrina made landfall on the Gulf Coast on August 29, 2005, with Hurricane Rita following on September 24, 2005. These two hurricanes caused major destruction and disruption in portions of Alabama, Louisiana, Mississippi, and Texas.

OCC is the primary regulator of all national<sup>2</sup> banks. Its mission is to charter national banks, oversee a nationwide system of banking institutions, and assure that national banks are safe and sound, competitive and profitable, and capable of serving in the best possible manner the banking needs of their customers.

To assure functions essential to accomplishing its mission could be performed during and in the aftermath of an emergency, OCC developed an Emergency Management Handbook

---

<sup>2</sup> In this report, the terms banks and national banks are used interchangeably, as all banks regulated by OCC are national banks.

---

consisting of emergency management procedures and Continuity of Operations (COOP) plans, including COOP plans for OCC's headquarters, district offices, field, satellite, and large bank offices.<sup>3</sup> OCC's emergency procedures distinguish between market events and emergency events. While both may affect the safety and soundness of national banks, OCC defines a market event as a disruption in the normal operation of any domestic or global market that could result in meaningfully elevated risk exposures to a national bank company, group of companies, or the banking system as a whole, and an emergency event as a disruption of lesser impact that OCC needs to monitor for supervision or reporting purposes. OCC considered Hurricanes Katrina and Rita to be emergency events and not market events. OCC used their Emergency Event Procedures during and immediately following the hurricanes, to capture reports on operational assessments of national banks operating in and close to areas affected by Hurricanes Katrina and Rita.

OCC, other federal financial institution regulators, and the Federal Financial Institutions Examination Council (FFIEC)<sup>4</sup> issued information that addressed a variety of issues that arose after the hurricanes. The topics covered included assistance to affected customers, availability of additional supervisory guidance on regulatory and reporting issues, availability of Community Reinvestment Act consideration for bank activities that revitalize or stabilize designated disaster areas,<sup>5</sup> and examination guidance for regulatory personnel for financial institutions affected by Hurricane Katrina.<sup>6</sup>

---

<sup>3</sup> OCC headquarters is in Washington, D.C. and four district offices: the Central District office in Chicago, Ill.; the Southern District Office in Dallas, Tex.; the Western District office in Denver, Co.; and the Northeastern District office in New York, N.Y. The OCC also has 52 field offices and 25 satellite locations in cities throughout the U.S., and resident examiner teams in the 23 largest banking companies.

<sup>4</sup> FFIEC is an interagency body empowered to prescribe uniform principles, standards, and report forms for the federal examination of financial institutions by the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the OCC, and the Office of Thrift Supervision (OTS).

<sup>5</sup> Joint Release of the FRB, FDIC, and OCC, "Banking Agencies Issue Final Community Reinvestment Guidance" (Mar. 2, 2006).

<sup>6</sup> OCC Bulletin 2006-5, federal financial institutions regulatory agencies and the state supervisory authorities in Alabama, Louisiana, and Mississippi jointly issued, "Hurricane Katrina: Guidance to Examiners" (Feb. 3, 2006).

---

FFIEC-issued guidance specifically intended to help financial institutions recover from the hurricanes addressed such topics as granting extensions to financial institutions for filing third-quarter Consolidated Reports of Condition and Income (Call Reports);<sup>7</sup> permitting financial institutions to use estimates to determine their loan loss reserves for their third quarter Call Reports until a determination on the collectibility of loans was confirmed; allowing financial institutions, for liquidity purposes, to immediately sell securities designated as held to maturity,<sup>8</sup> and exempting institutions from real estate appraisal requirements for real estate transactions in designated counties affected by the hurricanes.<sup>9</sup>

OCC coordinated with banks' technology service providers, worked with the United States Postal Service on mail service issues, and posted information, including frequently asked questions, on its Web site to help banks and consumers affected by the hurricanes.

OCC also conducted a lessons learned review of the hurricanes to address future emergencies. In particular, the review identified the importance of alternate means of communication, such as satellite telephones, resulting in OCC's purchase of satellite telephones for all of its field offices. OCC is considering encouraging banks to do the same.

OCC categorizes national banks as large, midsize, or community. OCC's community banks are generally defined as banks with less than \$1 billion in assets. OCC conducted operational assessments on 48 community banks following the hurricanes between August 30, 2005, and October 12, 2005. The operational assessments covered major areas such as bank

---

<sup>7</sup> National banks are required to file quarterly Call Reports, which contain detailed information about the bank's operations and financial condition. Reports are due on the 30<sup>th</sup> day after the end of each calendar quarter. However, banks with a foreign office(s) have 40 days after the end of each calendar quarter to file.

<sup>8</sup> "FFIEC Agencies Announce Additional Guidance for Financial Institutions in Response to Hurricanes Katrina and Rita" (FFIEC press release, Oct. 6, 2005).

<sup>9</sup> In OCC Bulletin 2005-36, FRB, FDIC, OTS, NCUA, and OCC jointly issued, "Real Estate Appraisal Exemptions in Major Disaster Areas" (Oct. 14, 2005).

---

closings, bank staffing issues, cash shipments to banks, and transaction processing issues.

On October 13, 2005, OCC categorized 12 community banks as at risk based on their lending exposure in areas most affected by the hurricanes. Of the 12 banks, 8 were considered affected by Hurricane Katrina and 4 by Hurricane Rita. OCC contacted the at risk banks to collect information on their financial condition and subsequently conducted analyses that covered the financial effects of the hurricanes on the banks' CAMELS ratings.<sup>10</sup> Assets and deposits of the at risk community banks totaled \$2.6 billion and \$2.1 billion, respectively. As of December 31, 2005, these 12 at risk community banks had increased their loan loss reserves in the preceding 6 month period by a combined total of \$5.8 million, representing 2.4 percent of the combined June 30, 2005, capital level for the banks.<sup>11</sup> The increase to loan loss reserves compared to capital was therefore not significant.

## Findings and Recommendations

Emergencies pose serious risks to the safety and soundness of banks. Short term, the risks are primarily to the banks' operations while long term, the risks are primarily to the banks' financial condition. OCC's supervisory responsibility to determine the banks' safety and soundness is therefore important following emergencies.

---

<sup>10</sup> The Uniform Financial Institutions Rating System was adopted by the FFIEC on November 13, 1979. The rating system, called CAMEL, was used to evaluate the safety and soundness of a savings association or a bank. On January 1, 1997, the rating system referred to as CAMEL became CAMELS. CAMELS is an acronym for the six component elements that are evaluated: capital, asset quality, management, earnings, liquidity and sensitivity to market risk. Each of these elements is rated on a scale of 1 to 5.

<sup>11</sup> A financial institution's loan loss reserve is an estimate of the amount needed to offset possible losses on loans. After the hurricanes, financial institution's estimated the storm related losses to their loan portfolios and increased loan loss reserves to cover the estimated losses.

---

## **Improvements Could be Made to OCC's Guidance to Assess the Financial Condition of At Risk Banks Following Emergencies**

We found that although OCC has specific procedures to follow when market disruptions occur, it lacks equivalent procedures for emergency events. OCC's market disruption procedures state that their objective is to ensure that within hours of a market disruption event, OCC's executive management and key staff has an assessment of the event that includes an opinion on the immediate and anticipated effects on the safety and soundness of individual companies as well as the National Banking System.<sup>12</sup> OCC's COOP plan for its Committee on Bank Supervision states that OCC's first critical function starting on the second day after a market disruption event is to continue to assess and report on the condition of the national banks. In contrast, OCC's Emergency Event Procedures do not contain timeframes by which OCC should assess and report on the condition of banks after emergency events, such as Hurricanes Katrina and Rita. OCC also has crisis management procedures that call for the creation of a crisis management team to be activated during an emergency event.<sup>13</sup> The objective of these procedures is to ensure that appropriate OCC action is taken as expeditiously as possible, although no timetable is specified within the procedures.

OCC identified 12 community banks as at risk based on their lending exposure in areas most affected by the hurricanes. Of these 12 banks, 8 were affected by Hurricane Katrina and 4 by Hurricane Rita. OCC initially obtained assessments from the banks affected by Katrina within days after that hurricane. While these assessments were primarily operational, they did touch on the immediate liquidity needs of the banks. OCC informed us that they tried to obtain financial information from the banks in late September 2005 to enable them to make financial assessments of the banks' conditions. However, the earliest documented evidence of financial information on asset

---

<sup>12</sup> OCC, Market Disruption Procedures and Checklist, "Emergency Management Handbook," (updated Sep. 2, 2003).

<sup>13</sup> OCC, Crisis Management Procedures, (issued Feb. 10, 2006).

---

quality and earnings from 11 of the 12 community banks was October 13, 2005, 45 days after Katrina's landfall and 19 days after Rita's landfall. This first summary information was prompted by a request from the Comptroller of the Currency on October 12, 2005, who was responding to an inquiry from the White House. Specifically, the request asked for an OCC determination of which banks might experience problems that would significantly affect capital and for an assessment of the financial impact. OCC provided the summary information to OCC Headquarters on October 14, 2005, and subsequently updated it on November 25, 2005. OCC stated in a November 27, 2005 internal communication that it would have a better understanding of banks' loss exposure in the 1<sup>st</sup> quarter of 2006. While not making formal risk assessments,<sup>14</sup> OCC staff informed us that they used the summaries as financial assessments and, based on the information provided by the banks, determined that the risk to the banks was not substantial following the hurricanes. As a result, OCC decided it was not necessary to further update the summaries. The continuation of OCC's supervisory process led to OCC completing quarterly analysis reports or full scope examination reports on these 12 banks. On average, it took OCC 4 ½ months following the hurricanes to complete these reports.

Unlike the standardized questionnaire OCC used to obtain operational assessments following Hurricane Katrina, OCC used narrative summaries to describe the financial condition of its banks. In its October and November 2005 summaries, the type of information covered was inconsistent. Some bank summaries included capital information and others did not. For example, in the October 13, 2005 summary, OCC's narrative summary for one bank included the following statement about capital, "Demand deposit accounts were up from 32 million dollars before to 53 million dollars after the storm and that has driven capital down to 7.3%". In contrast, its summary for another bank was less specific about the impact of the storm to capital, "No huge individual loan losses. Expect some losses to come

---

<sup>14</sup> To ensure effective supervision of community banks by risk, the OCC requires a common framework to document decisions about risk. The Risk Assessment System (RAS) provides a concise method of communicating and documenting judgments regarding the quantity of risk, the quality of risk management, the level of supervisory concern and the direction of risk.

---

from deficiency balances after insurance payoffs. Expect a spike in bankruptcies. Bank has given 400 extensions...gave 90 day extensions across the board. Loan demand is high with \$4.5 million new loans in 3<sup>rd</sup> quarter 2005 not storm related...deposit growth...concerned about insurance companies fighting claims, not paying anything, and fighting between flood and hazard and bank and customer will be caught in the middle..."

By not using a structured or standardized approach to gathering financial condition information following an emergency, OCC might not obtain critical information about the banks' financial conditions for further analysis in a consistent manner.

### **Recommendations**

We recommend that the Comptroller of the Currency do the following:

1. Ensure that OCC modify its Emergency Event Procedures to require documentation and summarization of all important elements of financial condition for at risk banks in a consistent manner.
2. Ensure that OCC modify its Emergency Event Procedures to require that following such an event, OCC determine and establish appropriate timeframes based on the gravity of the situation, for analyzing the effects on at risk banks financial condition.

### **Management Response**

In its response, provided in appendix 2, OCC noted that its actions flowed from its risk-based approach to supervision. OCC plans to respond to recommendations (1) and (2) by fully reflecting this risk-based approach to supervision in its Emergency Event Procedures, by July 31, 2007. OCC also expressed a concern that the report may give the impression that OCC did not take appropriate responsive action to Hurricanes Katrina and Rita, as opposed to not fully document its action.

---

### OIG Comment

To the extent that the modification to the Emergency Event Procedures leads to documentation and summarization of the financial condition of at risk banks and addresses the establishment of timeframes after disasters, the corrective action will be responsive to recommendations (1) and (2). OCC is correct that our report's main focus is on improvements to documentation rather than on actions taken by OCC, as the documentation we reviewed did not allow for a clear determination of when elements of the condition of at risk banks were established.

### **Improvements Could be Made to OCC's Operational Assessment Process for Community Banks Following Emergencies**

OCC Southern District Office guidance states that the Field Office Assistant Deputy Comptroller is responsible for identifying national banks that may have been affected by a disaster, that the District Deputy Comptroller is responsible for requesting regular status reports on the situation and the impact on banks in a disaster area, and for communicating banks' status to appropriate OCC management. The guidance further states that the Field Office Assistant Deputy Comptroller is responsible for coordinating with the field office staff and portfolio managers to conduct an efficient and effective assessment of the disaster's impact on and damage to banks, and contacting the District Deputy Comptroller when they can not account for a bank.<sup>15</sup> Additionally, guidance found in OCC Emergency Event Procedures calls for reports of impact on OCC-supervised banks.

Also, under the FFIEC "Supervisory Emergency Communication Protocols,"<sup>16</sup> each FFIEC member agency is to establish and maintain the capability of rapidly communicating during

---

<sup>15</sup> OCC, "Southern District Disaster Guidance and Emergency Response", *Southern District Risk Tip*, (dated Aug. 31, 2004).

<sup>16</sup> FFIEC, "Supervisory Emergency Communication Protocols", (updated Mar. 31, 2005).

---

emergencies with the institutions over which it has primary supervisory authority.

If OCC is not able to identify a distinct universe of banks in or close to disaster areas, OCC increases the risk that it will not be able to communicate with the banks effectively during an emergency and without documentation of communication with banks in or close to an affected area, OCC management cannot be assured that banks were contacted as appropriate.

We found the following areas where OCC could strengthen its ability to assess risk following emergency events:

- Documentation of contact with community banks in areas affected by an emergency event and identification of banks in these areas.
- Communication with community banks following emergency events.

**OCC could not provide evidence of contact with all community banks in areas affected by Hurricane Rita and weaknesses existed in the identification of banks in these areas**

While Hurricane Rita's impact was significantly less than Hurricane Katrina's impact, OCC stated in internal communication that it had contacted all the community banks in areas affected by Hurricane Rita. However, OCC was not able to provide documented evidence of contact with all community banks on lists prepared by OCC in anticipation of Hurricane Rita. OCC's division of Supervision provided us with 2 different lists of banks that had been developed by 2 separate areas within OCC in anticipation of Hurricane Rita. One list identified 52 community banks in or close to the forecasted path of Rita, while the other identified 33. In OCC's lessons learned review for the hurricanes, OCC identified duplicative efforts in developing lists of banks affected by Katrina and Rita as an area to be improved.

Adjusting for additional banks subsequently identified by OCC as well as for banks in areas where OCC judged that Rita had had no impact and therefore did not contact, OCC agreed that it

---

did not have documented evidence of contact with 5 banks using the first list or 3 banks using the second list. We also found that 4 banks should not have been on the first list as they were either no longer regulated by OCC as a result of liquidation or merger or had merged with other OCC-regulated banks on the list, with 1 of these also incorrectly identified on the second list. FDIC requested a list of banks that OCC had contacted for Hurricane Rita. An official from OCC's Southern District office responded that he did not have an accurate list of all the banks contacted by the field offices.

### **OCC Had Difficulty Establishing Communication with Community Banks Following Hurricane Katrina**

OCC had difficulty establishing communication with community banks following Hurricane Katrina as its communication efforts were hampered by power and telephone outages, also, OCC often did not have alternate contact information for bank personnel. In preparation for Hurricane Rita, OCC enhanced its communication efforts with banks by taking steps such as broadly disseminating the telephone number for the Southern District office and personal telephone numbers for officials who were out of the path of the hurricane.

OCC contacted 32 community banks, operating in or close to areas affected by Katrina, which it believed at risk. OCC contact information for banks consists primarily of bank office telephone numbers and bank office e-mail addresses. An OCC New Orleans field office official stated that OCC needed bank contact numbers and e-mail addresses outside of the banks and that communication attempts should be made by both OCC and the banks.

OCC's contact effort was a coordinated one, involving OCC staff from several Southern District field offices. Based on the dates of communication provided by OCC, initial contact was made within 1 or 2 days following the hurricanes for the majority of the banks. It took 8 days to contact 2 of those banks. In some instances, before making direct contact, OCC had obtained information on banks' operational conditions

---

through secondary sources such as other bankers, a banks' data processing service provider, and local officials.

### **Recommendations**

We recommend that the Comptroller of the Currency do the following:

3. Ensure that OCC document its contact made with individual banks following an emergency event and develop a methodology to accurately identify banks to be monitored in emergency events.
4. Ensure that OCC maintains current alternative contact information for banks and alternative channels of communication for use by OCC personnel to contact banks during emergencies. OCC should also consider encouraging banks to contact OCC during emergencies and provide banks alternative OCC contact information to facilitate communications.

### Management Response

In its response, OCC stated that while their bank supervision procedures require documentation of significant events, it believes that its documentation of significant events affecting its banks could be improved. In response to recommendation (3), OCC stated that it has conveyed this to its senior district management. OCC plans to respond to recommendation (4) by ensuring that its systems include alternative contact information by August 31, 2007. Whenever possible, OCC plans to contact its institutions prior to an emergency, ensure bankers also have alternative contact information for OCC and encourage banks to contact OCC if necessary. OCC also commented that at no time was it unaware of either storm's effect on its institutions, their markets, or their communities.

### OIG Comment

To the extent that OCC clearly conveys to senior district management its belief that its documentation of significant

---

events needs improvement, the corrective action will be responsive to the first part of recommendation 3. However, OCC's response did not address the second part of recommendation 3 which is to develop a methodology to accurately identify banks to be monitored in emergency events. We believe such a methodology is important as OCC identified duplicative efforts in developing lists of banks affected by Katrina and Rita as an area to be improved.

OCC's agreement to ensure its systems include alternative contact information for bank personnel by August 31, 2007, is responsive to recommendation 4.

We were unable to substantiate OCC's assertion that at no time was it unaware of either storm's effect on its institutions, since as noted this report, OCC agreed that it did not have documented evidence of contact with several banks after hurricane Rita and it took OCC 8 days to contact 2 banks after Katrina.

\* \* \* \* \*

We appreciate the courtesies and cooperation provided to our staff during the audit. If you wish to discuss this report, you may contact me at (202) 927-0382. Major contributors to this report are listed in appendix 4.

Alain Dubois  
Director, Banking Audits

Our audit objectives were to (1) determine the preparedness for and responsiveness of OCC with respect to addressing the needs of banks and their customers during Hurricanes Katrina and Rita and (2) determine OCC's plans and abilities to assess and manage increased risks to banks following the hurricanes. We focused our audit on OCC's supervision of community banks because, with the exception of one large bank and one midsize bank, all affected banks determined to be at risk by OCC were community banks.

To accomplish these objectives, we performed the following activities:

- Conducted interviews with OCC headquarters personnel in Washington, DC, the OCC New Orleans Field Office, and OCC midsize and large bank examiners
- Reviewed OCC documentation for information gathered from OCC personnel regarding banks related to the hurricanes
- Reviewed OCC's completed Reports of Examination and quarterly analyses for 12 at risk community banks
- Reviewed headquarters, district office, and field office COOP plans in OCC's Emergency Management Handbook

We performed our fieldwork from November 2005 through January 2007. We performed our audit in accordance with generally accepted government auditing standards.

Appendix 2  
Management Response



---

Comptroller of the Currency  
Administrator of National Banks

---

Washington, DC 20219

May 9, 2007

Mr. Alain Dubois  
Director, Banking Audits  
Department of the Treasury  
Office of Inspector General  
740 15<sup>th</sup> Street, NW  
Suite 600  
Washington, D. C. 20220

Dear Mr. Dubois:

We have received and reviewed your draft report "OCC Could Further Strengthen Its Ability to Assess Risks to Community Banks Following Emergencies." Hurricanes Katrina and Rita were so devastating that we certainly share the concerns that prompted your review of the OCC's handling of emergency events.

The OCC routinely examines the adequacy of our response in the wake of emergency events in order to learn from the experience gained. We attempt to draw conclusions about the effect the emergency has had on our institutions and our expectations of our examiners and staff during and immediately after an emergency. If necessary, we make adjustments to our emergency event procedures. For example, between these storms, we provided examiners with an additional means of communication to compensate for the possible unavailability of land-based services in the future.

We had difficulty establishing communication with all community banks following Katrina, a universal issue faced by everyone trying to establish communications in the disaster zone immediately following the storm. OCC examiners and managers contacted each bank as soon as possible following that storm's landfall, working under difficult conditions and in some cases resorting to extraordinary measures. Prior to Rita's landfall, our examiners or their managers contacted each bank in communities that had the potential to be affected. Following the storm, additional calls were made to the banks in communities that had, in fact, been affected. At no time were we unaware of either storm's effect on our institutions, their markets, or their communities.

Despite the agency's actions and responses, you concluded that further improvements could be made to OCC's guidance to assess the financial condition of at-risk community banks, and to OCC's operational assessment process for community banks following emergencies. We are concerned that readers of your report may draw an inaccurate conclusion about the OCC's

## Appendix 2 Management Response

---

response to Hurricanes Katrina and Rita because your conclusions are less a reflection that work was not done than that actions were not fully documented in OCC supervisory reporting systems.

Notwithstanding these concerns, we do plan to respond to the four recommendations offered for our consideration. In the category "Assessing Financial Condition," you recommend that we modify Emergency Event Procedures to require:

- documentation and summarization of all important elements of financial condition for at-risk banks in a consistent manner; and
- that following such an event, OCC determine and establish appropriate time frames, based on the gravity of the situation, for analyzing the effects on at-risk banks' financial condition.

As we explained during the course of the audit, our approach to supervision for safety and soundness is continuous, and it is based on risk. We routinely perform risk assessments that look at a standard list of categories and make a determination as to which areas pose a threat to the ongoing safety and soundness of individual institutions. These assessments are revisited periodically and are coupled with a quarterly evaluation of the financial condition based on official financial reports -- call reports -- that the banks file on a common date. For all community banks, the results of these assessments and analyses are documented in Examiner View.

Our actions with respect to the community banks affected by either or both storms flowed from our risk-based approach to supervision. Our assessments were based on the risks faced by each bank, and our actions were tailored accordingly. Our approach was consistent among banks even though the time frames involved, the amount of information obtained, and the nature of that information differed from bank to bank.

To fully reflect this approach in our Emergency Event Procedures, by July 31, 2007, we will modify those procedures to incorporate by reference the policies and procedures that describe our risk-based approach to supervision.

In the category "Assessing Operations," you are recommending that the OCC:

- document its contact made with individual banks following an emergency event and develop a methodology to accurately identify banks to be monitored in emergency events; and,
- maintain current alternative contact information for banks and alternative channels of communication for use by OCC personnel to contact banks during emergencies. OCC should also consider encouraging banks to contact OCC during emergencies and provide banks alternative OCC contact information to facilitate communication.

Our bank supervision procedures require documentation of significant events impacting our banks in Examiner View, our system of record for community bank information. This documentation may take several forms, including an Other Significant Event or mention within

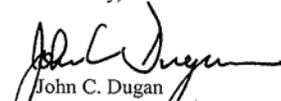
Appendix 2  
Management Response

---

the context of a Periodic Monitoring Report. Notwithstanding this, documenting all aspects of actions and thought processes so that a third party can precisely reconstruct each and every detail runs counter to the notion of recording significant events and deploying available resources to focus on the risks those events represent. Nevertheless, we believe that our documentation of significant events affecting our banks could be improved, and this has been conveyed to our senior district management. We will also ensure our systems include alternative contact information by August 31, 2007. When it is possible to contact our institutions prior to an emergency (such as the pending landfall of a major hurricane), we will ensure that the bankers also have alternative contact information for us and will encourage them to contact us if they believe it necessary.

Thank you for providing us the opportunity to comment on this draft report. Should you need additional information, please do not hesitate to contact me.

Sincerely,



John C. Dugan  
Comptroller of the Currency

Appendix 3  
Major Contributors To This Report

---

Alain Dubois, Director, Banking Audits  
Bobbie Gambrill, Auditor  
Vicky Liu, Program Analyst  
Esther Tepper, Communications Analyst  
Maryann Costello, Referencer

**Department of the Treasury**

Office of Accounting and Internal Control  
Office of Strategic Planning and Performance Management

**Comptroller of the Currency**

Comptroller of the Currency  
Liaison Officer

**Office of Management and Budget**

OIG Budget Examiner